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C O N F I D E N T I A L SECTION 01 OF 03 CARACAS 000193

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SUBJECT: Chevron "Wins" A Carabobo Project

REF: 10 CARACAS 11

CLASSIFIED BY: Darnall Steuart, Economic Counselor, DOS, Econ;
REASON: 1.4(B), (D)

11. (C) SUMMARY: Chevron and Repsol-led consortia won the rights to negotiate mixed company deals with the Ministry of Energy and Petroleum (MENPET) in the Carabobo bid round. In its first major heavy oil bid round since President Chavez assumed power in 1999, the Bolivarian Republic of Venezuela (GBRV) offered three Carabobo projects and received bids on two. While not signing any agreements, the winning international consortia may now move ahead to negotiate more favorable contract terms before signature of a joint venture contract and the initial bonus payment. Chevron said that first oil might come on line in 2014 but could well be delayed. The Ambassador was not invited to the Carabobo ceremony to accompany his colleagues representing the governments of the other international oil companies that bid. Nevertheless, at the ceremony, Chavez said he wants dialogue with the U.S. END SUMMARY.

Carabobo Winners Announced

12. (C) PROJECT 3: The February 10 ceremonial event to announce the winners in the Carabobo bid round started several hours late and was televised in a mandatory national cadena (broadcast). The Chevron-led consortia, including Japan's Mitsubishi, Inpex, and Venezuela's Suelopetrol, won project 3, which includes blocks C5, C2 South, and C3 North. Chevron's share in the ultimate joint venture will be 34%, the Japanese participants will have 5%, and Suelopetrol will have a 1% share. [NOTE: Chevron's Latin America Business Unit President Wes Lohec (protect) told the Ambassador on February 12 that Japan's JOGMC has an option to back into a share of the Japanese 5%. The Japanese participation in the consortium is particularly important, as it will open the door to possible JBIC financing for PDVSA's portion of the project costs. END NOTE] Minister Ramirez stated that the mixed company (60% PDVSA, 40% Chevron consortia) should eventually produce between 400,000 and 480,000 barrels of crude petroleum per day. When half of the production is run through an upgrader and mixed with the other half of production, the mixed company will ultimately take 400,000 barrels of 22-degree API crude to the market. Ramirez stated that

the Chevron consortium offered a bonus of \$500 million, a billion dollars of financing for PDVSA's portion of the project, and an upgrader to be constructed in Soldedad. Lohec informed the Ambassador on February 12 that cold crude oil production could begin as soon as four years from the date a mixed company is formed and that MENPET had committed to provide 300 million barrels of blending stock for the first seven years of the project or until an upgrader is constructed. Lohec added that he doubted whether PDVSA would achieve any new petroleum production from any of the various heavy oil projects it has initiated with national oil companies before 2014.

13. (U) PROJECT 1: Ramirez also announced that the consortium led by Spain's Repsol, including India's ONGC, Videsh Limited, Oil Indian Corporation, the Indian Oil Corporation, and Malaysia's Petronas, won Carabobo's project 1. This includes the blocks C1 North, and C1 Central. According to Ramirez, Repsol's consortium offered a bonus of \$1.050 billion, \$1.0 billion in financing for PDVSA's portion of the project, and an upgrader in Soledad. Ramirez stated that this mixed company would also produce up to 480,000 barrels/day of upgraded petroleum at 22 degrees API. Repsol's proposal included plans to send some of the upgraded petroleum to a refinery in Bilbao, Spain and "other plants in other countries." Ramirez stated that the mixed company agreements now to be negotiated with the two consortia would be sent to the Venezuelan National Assembly for approval on March 25.

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14. (U) PROJECT 2: According to Ramirez, the GBRV did not receive any offers on project 2 and that it would be up to President Chavez whether Venezuela would develop it on its own or put it back out to bid in the future.

15. (C) BONUS?: Chevron's consortium offered the minimum bonus for project 3 (the other two projects had a minimum bonus of \$1 billion). Repsol's consortium offered \$50 million more than the minimum bonus payment. Given that project 3 (Chevron) contained three blocks and project 1 (Repsol) contained two blocks, the consortia respectively offered \$167 million/block and \$500 million/block. By contrast, in the bilateral deals announced by the GBRV for heavy oil projects in the Junin area of the Orinoco heavy oil belt, the press has reported that Italy's Eni offered a \$646 million bonus for Junin 5, PetroVietnam offered a bonus between \$500 and \$600 million, and the Russian oil consortium (Rosneft, Lukoil, Gazprom, TNK-BP, and Surgutneftegaz) offered \$1 billion for Junin 6. Embassy contacts reiterate that, regardless of the GBRV announcements, no company has yet made a bonus payment to the GBRV. The Carabobo terms require the first installment of the bonus payment 14 days after the mixed company documents are approved by the international consortia's boards of directors and by the Venezuelan National Assembly. Thus, the GBRV will not receive any bonus funds from the Repsol or Chevron-led consortia until the mixed companies have been negotiated and approved.

16. (C) Mixed Company Formation: On February 11, Chevron President for Africa and Latin America Ali Moshiri clarified for the Ambassador that the winning consortia had not won blocks or projects, but rather the right to negotiate an agreement to form mixed companies to produce crude oil. He described the February 10 ceremony presided over by President Chavez as a "symbolic event" and said that meeting the March 25 deadline for submission of the mixed company agreement to the National Assembly would be "magic." He noted that on Chevron's part, any agreement would have to be approved by its Executive Committee and Board of Directors. Given that its Board of Directors meets monthly, it would be unrealistic for Chevron to approve a mixed company deal before March 25. Many unresolved issues remain to be negotiated, including royalty and tax rates, windfall profits taxes, shadow tax payments, etc. (see Reftel). The GBRV wants the upgraders constructed in Soledad, but Moshiri said that the geographic location of Soledad makes the

economics of the upgrader untenable. He noted that he has talked to Chavez privately about this issue.

17. (C) To Bid or Not to Bid: Lohec described Chevron's basic calculus on whether or not to bid on Carabobo as an assessment of the likelihood of success in future negotiations with the GBRV. Chevron believes "it has a strong hand to play to get to where we need to be," said Lohec, a decision that other companies could not make. He added that Chevron is confident it will successfully negotiate favorable terms for the formation of a mixed company with PDVSA. Lohec added that MENPET has already agreed to allow the new mixed company to lift crude petroleum shipments as dividend payments (a scheme Chevron has developed over the past year in its mixed company operating PetroBoscan). He noted that due to the phased payment plan for the bonuses, Chevron will only pay MENPET \$100 million upon signing the documents to form a mixed company and that the other four installment payments are linked to project milestones, effectively limiting risk exposure. Lohec underlined that the GBRV needs Chevron's expertise because it "is headed down a path that is disastrous for them." In the end, the Venezuelans need to produce oil to generate revenue. Finally, Lohec noted that

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new projects in Iraq likely played into BP and Shell's calculus not to bid in Venezuela. Since Chevron does not have any projects in Iraq and is "already big in Venezuela," it decided to continue forward here. Separately, Lohec told Petroleum AttachC) that BP and Shell might decide to shut down operations in Venezuela - that it all depends on whether limited operations here are profitable or not and how long a timeline they are working with, noting that Shell usually works with a 20-year timeframe. Lohec added as an aside that Chevron continues negotiations to convert an exploration and certification project in the Ayacucho 8 block of the Faja into a production expansion adjacent to its current PetroPiar mixed company. [NOTE: Ayacucho 8 does not appear on recent PDVSA maps. END NOTE]

18. (C) Chevron's View on U.S.-Venezuelan Bilateral Relations: Moshiri expressed surprise that the Ambassador did not receive an invitation to the Carabobo announcement ceremony. [NOTE: Ambassadors or other diplomats from the home countries of the other winning oil companies attended the event. END NOTE] In his opening remarks in the televised portion of the event, President Chavez stated his desire to establish a dialogue with the U.S. administration. On the margins of the event, he noted to Moshiri his desire to see the Houston Astros play in Texas, but added that political realities make a visit to the U.S. impossible. [NOTE: In response, Moshiri offered a courtesy invitation for Chavez to visit Chevron in Houston. END NOTE] Moshiri told the Ambassador that Chevron would press the GBRV to extend an invitation to the Ambassador to attend any future signing ceremony for the mixed company deal. He also said he would raise the GBRV's failure to invite the Ambassador to the Carabobo ceremony the next time he spoke with Ambassador Alvarez. Moshiri noted, however, that he believes that Alvarez now has less access to Chavez. Finally, Moshiri said that Alvarez had made it clear that all decisions regarding the bilateral relationship with the U.S. are elevated to Chavez. The Ambassador underlined to Moshiri that the USG has made every effort to re-establish a dialogue with the GBRV. In fact, he said, the Embassy had been waiting for months for a response from the GBRV to Diplomatic Notes responding to GBRV interest in a dialogue on energy issues as well as the invitation from Energy Secretary Chu to attend the April Energy and Climate Ministerial of the Americas. Moshiri commented that Energy Minister Ramirez would not take the risk of responding to these initiatives without a decision from Chavez.

19. (C) Comment: The GBRV and media portrayals of the Carabobo ceremony are misleading as no deals were signed. With the leverage the international companies now have in negotiations with the GBRV,

we would not expect to see any deals signed by late March as the companies will take the time they need to secure favorable terms. A potential new Chevron deal would solidify its position as the GBRV's largest and most important international partner. Repsol has been a relatively minor partner with PDVSA and the Indian companies are not currently involved in any projects in Venezuela. Their lack of experience raises questions about the potential success and ability to move project 1 forward. In the event that new mixed companies are formed, it will be the first time the Chavez administration and its Energy Ministry and PDVSA have developed, executed, and operated a production project of this magnitude. Many here are skeptical about their ability to do so. In the past, Venezuela allowed the major international oil companies to engineer, build, and operate the projects. Since nationalization of the sector in 2007, PDVSA has failed to maintain and or expand production. END COMMENT.

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